



STATE OF MICHIGAN
DEPARTMENT OF TREASURY

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DATE: June 9, 2011

TO: Assessors and Equalization Directors

FROM: State Tax Commission

SUBJECT: The Michigan Supreme Court's Decision in *Klooster v City of Charlevoix*

The State Tax Commission rescinds the Klooster v City of Charlevoix case memo dated March 21, 2011 and replaces it with this document.

Summary of the Court Case:

On March 10, 2011, the Michigan Supreme Court issued a decision in the case of *Klooster v City of Charlevoix*, Michigan Supreme Court Docket No. 140423 (2011), regarding the interpretation of MCL 211.27a(7)(h) and specifically which conveyances involving a joint tenancy are or are not transfers of ownership.

James Klooster, the father, quit-claimed his property to himself and to his son, Nathan as joint tenants with rights of survivorship, on August 11, 2004. James died on January 11, 2005, leaving Nathan as the sole owner. On September 10, 2005, Nathan quit-claimed the property to himself and his brother, Charles, as joint tenants with rights of survivorship. The assessor uncapped the taxable value for the 2006 assessment year. The taxpayer appealed and the Tax Tribunal ruled that the taxable value should have uncapped for the 2006 assessment year because Nathan was not an "original owner," or an already existing joint tenant before the August 11, 2004 joint tenancy was created.

The Michigan Court of Appeals reversed the Tax Tribunal. The Court found the property should not have uncapped because the death of a joint tenant does not constitute a transfer of ownership, even if the joint tenant who dies was the sole original owner. The Court concluded that a "conveyance" within the meaning of MCL 211.27a(7)(h) could not occur unless there was a transfer of title by a written instrument.

The Michigan Supreme Court reversed the Michigan Court of Appeals decision. The Supreme Court found that the death of the only other joint tenant is a conveyance under the GPTA and does not require a written instrument beyond the deed initially creating the joint tenancy. The Court also determined that MCL 211.27a(7)(h) establishes requirements for an exception from the definition of transfer of ownership in three separate and distinct types of conveyances: termination of a joint tenancy, creation of a joint tenancy where the property was not previously held in joint tenancy or the creation of a successive joint tenancy.

Definitions:

Joint Tenancy: A joint tenancy is a form of concurrent ownership wherein each co-tenant owns an undivided share of property and the surviving co-tenant has the right to the whole estate. On the death of each joint tenant, the property belongs to the surviving joint tenants, until only one individual is left.

Initial Joint Tenant: A person whose interest in the property was obtained because he or she was one of the joint tenants who became a co-owner as a result of the “initial” joint tenancy **and** who has continuously held an interest in the property as a co-owner in joint tenancy since the creation of the “initial” joint tenancy.¹

Original Owner: A sole owner at the time of the last uncapping event; a joint owner at the time of the last uncapping event; or, the spouse of the either a sole or joint owner of the property at the time of the last uncapping event.

How to Determine if a Property Should Uncap:

Step 1: Identify the “Conveyance at Issue”

The first step is to determine if the “conveyance at issue” is the creation of an “*initial*” joint tenancy, the creation of a “*successive*” joint tenancy or the “*termination*” of a joint tenancy. The determination of whether a “conveyance at issue” is a transfer of ownership that uncaps the taxable value of the property must be separately determined *after* identification of the “conveyance at issue.” A conveyance will not constitute a transfer of ownership under the General Property Tax Act if it is excluded under MCL 211.27a(7)(a) through (q).

Step 2: Determine if the Conveyance is the Creation of a Joint Tenancy

The creation of an “initial” joint tenancy occurs when a property held by a sole owner, by a husband and wife holding as tenants by the entirety, or by tenants in common, is conveyed to two or more persons as joint tenants.

If the person creating the joint tenancy held title to the interest being conveyed either as a sole owner, as husband and wife, tenants by the entirety, or as tenants in common, then the creation of a joint tenancy is not a transfer of ownership, if, at least one of the persons conveying the interest **and** one of the persons receiving the interest was an “original owner.”

If you determine the conveyance meets the requirements defined above, **STOP**. No further review is necessary and the conveyance is not a transfer of ownership. If the conveyance does not meet both requirements defined above, move to Step 3 and/or Step 4.

¹ This phrase “initial joint tenant” is not specifically used in the Supreme Court’s decision, but is helpful in explaining the decision.

Step 3: Determine if the Conveyance “Terminates” a Joint Tenancy

A joint tenancy terminates when there is no “successive” joint tenancy. The termination of joint tenancy **is** a transfer of ownership if the resulting owner is not an “initial joint tenant.”

The termination of a joint tenancy **is not** a transfer of ownership if both of the following are true:

- At least one of the joint tenants in the joint tenancy being terminated was an “original owner” before the joint tenancy was initially created; **and**
- At least one of the joint tenants in the joint tenancy being terminated was an “initial joint tenant” and has remained a joint tenant in successive joint tenancies.

Step 4: Determine if the “Conveyance at Issue” is the creation of a “Successive” Joint Tenancy

A “successive” joint tenancy occurs when the conveyance is from one joint tenancy directly into another joint tenancy. The creation of a “successive” joint tenancy may, or may not, be a transfer of ownership.

The creation of a “successive” joint tenancy is **not** a transfer of ownership if both of the following are true:

- At least one of the individuals in the “successive” joint tenancy was an “original owner” **and**
- At least one of the joint tenants in the previous joint tenancy was an “initial joint tenant” and has remained a joint tenant in successive joint tenancies.

Conclusion:

- If a joint tenancy is created by an "original owner" and if that "original owner" or their spouse are also co-tenants in the joint tenancy, then the taxable value does not uncapse.
- If a "successive" joint tenancy is created and an "original owner" or their spouse continue as co-tenants in the "successive" joint tenancy, then the taxable value does not uncapse.
- If a joint tenancy is terminated by the death of an "original owner" or by the "original owner" making a conveyance, resulting in the ownership again being a sole ownership, and if that sole owner is an "initial joint tenant," then the taxable value does not uncapse.
- If a joint tenancy is terminated by conveyance and the sole owner after the termination is an "initial joint tenant" then the taxable value does not uncapse.

Several examples of each of the scenarios described above are listed below. The list should not be considered all inclusive. The State Tax Commission advises assessors that taxpayers are protected by a right of appeal, and therefore, when in doubt if a transfer of ownership should result in an uncapping, an assessor should consider uncapping the property.

Assessors are directed to MCL 211.27a(4) and Bulletin 9 of 2005 for the procedures to follow if they determine the taxable value has mistakenly uncapped for a past assessment year. General questions regarding transfers of ownership are addressed in the State Tax Commission Transfers of Ownership Publication available on the Commission's website under the What's New heading and the Publications link: www.michigan.gov/statetaxcommission. Specific questions regarding the Klooster Case and transfer of ownership can be directed to Heather Frick or Tim Schnelle at 517-335-3429.

Example # 1: Creation of a Joint Tenancy

John, who was a single man at all relevant times, purchased Blackacre in 2004. In 2005, John conveyed Blackacre to himself and his son, Michael, as joint tenants, with rights of survivorship. Did the taxable value uncapped in 2006?

No, there was not a transfer of ownership. Since there was a transfer of ownership which uncapped the taxable value when John purchased the property in 2004, John was an "original owner" who continued to have an interest after the creation of the joint tenancy. Michael became an "initial joint tenant" but he was not an "original owner." John's status as an "original owner" who continued to be a co-tenant as part of the "initial" joint tenancy provides an exception to uncapping. Michael's status as an "initial joint tenant" is not a factor in the analysis.

Example # 2: Termination of a Joint Tenancy

John, who was a single man at all relevant times, purchased Blackacre in 2004. In 2005, by quit claim deed, John conveyed to himself and his son, Michael, as joint tenants, with rights of survivorship. Several weeks later, but still in 2005, John died, leaving Michael as the sole surviving co-tenant. Did the taxable value uncapped in 2006?

No, there was not a transfer of ownership. Since John had previously held title as a sole owner, the joint tenancy he created with Michael was an "initial" joint tenancy. Further, since there was a transfer of ownership which uncapped the taxable value when John purchased the property in 2004, John was an "original owner." John was an "original owner" and an "initial joint tenant" when the joint tenancy was initially created in 2005. Further, John remained a joint tenant from the creation of the "initial" joint tenancy until the joint tenancy was terminated by the death of John. Since John was an "original owner" who continued to be a co-tenant after the creation of the "initial" joint tenancy and since Michael became a joint tenant when the "initial" joint tenancy was created, and Michael's interest continued uninterrupted until the death of John, the taxable value did not uncapped when John died.

Example # 3: Termination and a Non-Successive Joint Tenancy

John, who was a single man at all relevant times, purchased Blackacre in 2004. In 2005, by quit claim deed, John conveyed to himself and his son, Michael, as joint tenants, with rights of survivorship. Several weeks later, but still in 2005, John died, leaving Michael as the sole surviving co-tenant. Michael immediately conveyed to himself and his brother, Peter, as joint tenants, with rights of survivorship. Did the taxable value uncapped in 2006?

Yes, there was a transfer of ownership when Peter was added as a joint tenant. These facts are, in substance, those in the *Klooster* case itself. Since John was an "original owner" who continuously held his interest as a co-tenant in the joint tenancy since the joint tenancy was initially created and since Michael became an "initial joint tenant" when the "initial" joint tenancy was created, the taxable value did not uncapped when John died. However, when

Michael, as the sole surviving co-tenant, created the joint tenancy with his brother, Peter, the creation of the joint tenancy itself was an uncapping event for the reason that Michael was not an “original owner” at the time of the creation of the “initial” joint tenancy with Peter. The reason that Michael was not an “original owner,” was that he had not acquired his ownership interest in a transaction that resulted in an uncapping of the taxable value.

Example # 4: Successive Joint Tenancy

John, who was a single man at all relevant times, purchased Blackacre in 2004. In 2005, by quit claim deed, John conveyed to himself and his son, Michael, as joint tenants, with rights of survivorship. In 2006, John and Michael conveyed to themselves and Michael’s brother, Peter, as an additional joint tenant, thereby expanding the joint tenancy by making John, Michael and Peter, joint tenants, with rights of survivorship. Did the taxable value uncapse in 2007?

No, there was not a transfer of ownership. John was an “original owner” arising from the fact that he obtained his interest in the property by a conveyance that resulted in the uncapping of the taxable value. John and Michael became “initial joint tenants” when the “initial” joint tenancy was created in 2005. Since John was an “original owner” whose ownership interest has continued in the “successor” joint tenancy that added Peter, and since both John and Michael were “initial joint tenants” whose interests as co-tenants was continuous from the time of the “initial” joint tenancy, the taxable value did not uncapse when Peter was added.

Example # 5: Life Estate

John and Mary purchased Blackacre, as tenants by the entireties, in 2004. In 2005 John and Mary conveyed to themselves and Michael, using language which indicated that “all three (held title) as joint tenants.” However, in addition to creating the joint tenancy among the three of them, John and Mary also reserved a life estate for their joint lives. In 2006, both John and Mary died. Did the taxable value uncapse in 2007?

Yes, there was a transfer of ownership. Although John and Mary were “original owners” in Blackacre, arising from the fact that the taxable value uncapped in 2005, the year following their purchase, no “present” joint tenancy was created by the 2005 conveyance. Instead, the instrument, by reservation, created a Life Estate during their joint lives, with a remainder interest, in joint tenancy, among John, Mary and Michael. MCL 211.27a(7)(c) provides an exception to uncapping for a conveyance of property subject to a retained Life Estate “until the expiration or termination of the life estate...” Therefore, it is the State Tax Commission’s interpretation that a separate and distinct uncapping event, the expiration or termination of a retained life estate, occurred prior to the joint tenancy becoming a present interest and that this uncapping event took precedence over the exception to uncapping contained in MCL 211.27a(7)(h). MCL 211.27a(6) provides that a “transfer of ownership means the conveyance of title to or a present interest in property, including the beneficial use of the property, the value of which is substantially equal to the value of the fee interest.” In this example, by the time the remainder interest becomes a present interest, Michael was the sole owner of the property, not an “initial joint tenant.” It should also be noted that upon the death of John and Mary, Michael becomes an “original owner.”

Example # 6: Partial Interest

John, who was a single man at all relevant times, purchased Blackacre in 2004. In 2005, by quit claim deed, John conveyed to himself and his son, Michael, as joint tenants, with rights of survivorship. Several weeks later, but still in 2005, John died, leaving Michael as the sole surviving co-tenant. Michael immediately conveyed a 1% interest in the property to his daughter, Roberta, as a tenant in common. At the time, Roberta was a Michigan resident who resided on the property, and the conveyance was made for the purpose of allowing her to claim the Principal Residence Exemption. In 2007, Michael and Roberta conveyed to themselves, as joint tenants, with rights of survivorship. Did the taxable value uncap in 2008?

Yes, there was a transfer of ownership as to an undivided 99% interest in the property. The original 1% conveyed to Roberta in 2005 resulted (or should have resulted) in an uncapping of the undivided 1% interest which she received as a tenant in common. This uncapping made Roberta an “original owner.” However, she was an “original owner” of *only an undivided 1% interest*, as a tenant in common, with her father. When the joint tenancy interest was created, the effect was that Michael, as the sole surviving co-tenant of the previous joint tenancy with his father, John, could not rely on the fact that he was an “initial joint tenant” to exempt the conveyance of the undivided 99% interest he still held, for the reason that when the previous joint tenancy terminated, he was not an original owner. He was not an “original owner” for the reason that he had not acquired his remaining 99% undivided ownership interest in a transaction that resulted in an uncapping of the taxable value.

Please note, however, if multiple grantors hold as tenants-in-common, each tenancy-in-common interest must be analyzed separately, and it is possible for a partial uncapping to occur, for the reason that a person may be an “original owner” as to one tenancy-in-common interest, but not an “original owner,” as to the remainder of the tenancy-in-common interests in the property.